

17-1353

TAX TYPE: INCOME TAX

TAX YEAR: 2011, 2012

DATE SIGNED: 03/08/2019

COMMISSIONERS: J. VALENTINE, M. CRAGUN, R. ROCKWELL, L. WALTERS

GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

<p>TAXPAYER,</p> <p style="text-align: center;">Petitioner,</p> <p>v.</p> <p>AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION,</p> <p style="text-align: center;">Respondent.</p>	<p style="text-align: center;">INITIAL HEARING ORDER</p> <p>Appeal No. 17-1353</p> <p>Account No. #####</p> <p>Tax Type: Income</p> <p>Tax Years: 2011 & 2012</p> <p>Judge: Chapman</p>
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Presiding:

Kerry R. Chapman, Administrative Law Judge

Appearances:

For Petitioner: REPRESENTATIVE FOR TAXPAYER, Representative (by telephone)
TAXPAYER, Taxpayer (by telephone)

For Respondent: REPRESENTATIVE FOR RESPONDENT, from Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for an Initial Hearing pursuant to the provisions of Utah Code Ann. §59-1-502.5, on January 8, 2019.

TAXPAYER-1 (“Petitioner” or “taxpayer”) appealed Auditing Division’s (the “Division”) assessments of Utah individual income taxes for the 2011 and 2012 tax years. On July 20, 2017, the Division issued Notices of Deficiency and Estimated Income Tax (“First Statutory Notices”) to the taxpayer, in which it imposed taxes, 10% penalties for failure to timely file, 10% penalties for failure to timely pay, and interest (calculated through August 19, 2017),¹ as follows:

¹ Interest continues to accrue until any tax liability is paid. As will be discussed later in the decision, the Division has issued a second Statutory Notice for the 2011 tax year not to TAXPAYER alone, but to TAXPAYER and his wife, NAME-1. For ease of reference, the Commission may refer to TAXPAYER and

<u>Year</u>	<u>Tax</u>	<u>Penalties</u>	<u>Interest</u>	<u>Total</u>
2011	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$
2012	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$	\$\$\$\$\$

At the time the Division issued its First Statutory Notices, TAXPAYER had not filed a Utah income tax return for either of the 2011 and 2012 tax years. In these non-filing audits, the Division assessed TAXPAYER alone with a filing status of single and allowing only one exemption. After TAXPAYER filed his appeal, he and his wife filed 2011 and 2012 Utah returns with a filing status of married filing jointly. On these returns, the taxpayers claimed four exemptions, two for themselves and two for dependents.

TAXPAYER explained that the two dependents that he and his wife claimed on their 2011 and 2012 Utah returns were their two sons. The older son was born on January 28, 1992 (he turned 19 years old during the 2011 tax year); while the younger son was born on May 4, 1995 (he turned 16 years old during the 2011 tax year). TAXPAYER further explained that the older son began serving a church mission when that son was still 18 years old (i.e., prior to turning 19 years old on January 28, 2011) and that this son did not return from his mission until after 2011. If this is correct, the taxpayers' older son was on his church mission for all or nearly all of the 2011 tax year. During 2011, the taxpayers' younger son was living at the taxpayers' home.

The 2012 Utah return that the taxpayers filed is consistent with information shown on Internal Revenue Service ("IRS") records. As a result, the Division accepted the 2012 Utah return and canceled its 2012 non-filing audit (as reflected in the First Statutory Notice that was issued for the 2012 tax year). The parties agree that the taxpayers currently have a \$0 balance for 2012 Utah income tax purposes. As a result, the taxpayers' Utah tax liability for the 2012 tax year is no longer at issue.

As a result of the taxpayers' filing the 2011 Utah return, the Division has also canceled its 2011 non-filing audit (as reflected in the First Statutory Notice that was issued for the 2011 tax year). The Division, however, contends that the information that the taxpayers reported on their 2011 Utah return is inconsistent with IRS records because the IRS disallowed one of the two dependents that the taxpayers claimed on their

NAME-1 together as the "taxpayers."

2011 federal return. Specifically, the Division contends that the IRS disallowed the taxpayers' older son as a dependent for the 2011 tax year.

The 2011 IRS transcript that the Division proffered at the Initial Hearing is ambiguous. The transcript shows the number of the taxpayers' 2011 exemptions to be four, which would include exemptions for both of the sons that the taxpayers claimed as dependents. However, the transcript also shows a "federal taxable income" amount of \$97,926 that is derived, in part, by deducting only three exemptions from the taxpayers' federal adjusted gross income. Furthermore, the transcript shows that the taxpayers reported an incorrect Social Security number for their older son on their 2011 federal return.

Because of the IRS transcript, the Division has changed the taxpayers' 2011 Utah return to reflect only one dependent and three exemptions, and it has issued a second 2011 assessment to reflect this change. On May 14, 2018, the Division issued a Notice of Deficiency and Audit Change ("Second Statutory Notice") to the taxpayers, in which it imposed additional taxes and interest (calculated through June 13, 2018),² as follows:

<u>Year</u>	<u>Tax</u>	<u>Penalties</u>	<u>Interest</u>	<u>Total</u>
2011	\$\$\$\$\$	\$0.00	\$\$\$\$\$	\$\$\$\$\$

The Division proffered that the IRS may have disallowed the taxpayers' older son as a 2011 dependent because of the incorrect Social Security number that the taxpayers reported for him on their 2011 federal return. Regardless, the Division contends that until the taxpayers show that the IRS has allowed them to claim two dependents for the 2011 tax year, the Commission should find that the taxpayers are only entitled to claim one dependent for 2011 Utah tax purposes. For these reasons, the Division asks the Commission to sustain the 2011 assessment that it issued to both taxpayers, as reflected in the Second Statutory Notice.

The taxpayers proffered that they were under the belief that they had contacted the IRS and corrected the Social Security number that they had erroneously reported for their older son on their 2011 federal return. The taxpayers, however, could not remember who it was who contacted the IRS or when they contacted the

2 Again, interest continues to accrue until any tax liability is paid. No penalties were imposed in the

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IRS. In addition, the taxpayers proffered no letter or other documentation from the IRS to show that the IRS had accepted a correction of their older son's Social Security number. Furthermore, the taxpayers do not refute the Division's claim that the "federal taxable income" reflected on the 2011 IRS transcript is based on the taxpayers' only being allowed to claim one dependent. Regardless, the taxpayers claim that they should be allowed to claim both of their sons as dependents for 2011 Utah tax purposes because they were allowed to claim both of their sons as dependents for tax years both before and after the 2011 tax year. For these reasons, the taxpayers ask the Commission to accept the 2011 Utah return that they filed and to reverse the Division's 2011 audit, as reflected by the Second Statutory Notice.

APPLICABLE LAW

Utah Code Ann. §59-10-103 (2011)³ defines "adjusted gross income" and "'taxable income' or 'state taxable income,'" as follows:

- (1) As used in this chapter:
 - (a) "Adjusted gross income":
 - (i) for a resident or nonresident individual, is as defined in Section 62, Internal Revenue Code; or
 -
 - (f) "Federal taxable income":
 - (i) for a resident or nonresident individual, means taxable income as defined by Section 63, Internal Revenue Code; or
 -
 - (w) "Taxable income" or "state taxable income":
 - (i) . . . for a resident individual, means the resident individual's adjusted gross income after making the:
 - (A) additions and subtractions required by Section 59-10-114; and
 - (B) adjustments required by Section 59-10-115;
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UCA §59-10-1018 authorizes a taxpayer to claim a nonrefundable tax credit against Utah income taxes otherwise due for amounts of standard or itemized deductions and personal exemptions, as follows in pertinent part:

Second Statutory Notice that the Division issued for the 2011 tax year.

3 The 2011 version of the substantive Utah law is cited in the decision.

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- (2) Except as provided in Section 59-10-1002.2, and subject to Subsections (3) through (5), a claimant may claim a nonrefundable tax credit against taxes otherwise due under this part equal to the sum of:
- (a) (i) for a claimant that deducts the standard deduction on the claimant's federal individual income tax return for the taxable year, 6% of the amount the claimant deducts as allowed as the standard deduction on the claimant's federal individual income tax return for that taxable year; or
 - (ii) for a claimant that itemizes deductions on the claimant's federal individual income tax return for the taxable year, the product of:
 - (A) the difference between:
 - (I) the amount the claimant deducts as allowed as an itemized deduction on the claimant's federal individual income tax return for that taxable year; and
 - (II) any amount of state or local income taxes the claimant deducts as allowed as an itemized deduction on the claimant's federal individual income tax return for that taxable year; and
 - (B) 6%; and
 - (b) the product of:
 - (i) 75% of the total amount the claimant deducts as allowed as a personal exemption deduction on the claimant's federal individual income tax return for that taxable year; and
 - (ii) 6%.
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For the instant matter, UCA §59-1-1417(1) (2019) provides guidance concerning which party has the burden of proof, as follows:

- (1) In a proceeding before the commission, the burden of proof is on the petitioner except for determining the following, in which the burden of proof is on the commission:
- (a) whether the petitioner committed fraud with intent to evade a tax, fee, or charge;
 - (b) whether the petitioner is obligated as the transferee of property of the person that originally owes a liability or a preceding transferee, but not to show that the person that originally owes a liability is obligated for the liability; and
 - (c) whether the petitioner is liable for an increase in a deficiency if the increase is asserted initially after a notice of deficiency is mailed in accordance with Section 59-1-1405 and a petition under Part 5, Petitions for Redetermination of Deficiencies, is filed, unless the increase in the deficiency is the result of a change or correction of federal taxable income:
 - (i) required to be reported; and
 - (ii) of which the commission has no notice at the time the commission mails the notice of deficiency.

DISCUSSION

Pursuant to Subsection 59-1-1417(1), the taxpayers have the burden of proof in this matter. The only matter still at issue is whether the taxpayers are entitled to claim one or two dependents for 2011 Utah income

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tax purposes. Subsection 59-10-1018(2)(b) authorizes a taxpayer to claim a nonrefundable tax credit against Utah income taxes otherwise due for certain amounts of the personal exemptions allowed on the taxpayer's federal income tax return. It is unclear from the IRS transcript of the taxpayers' 2011 federal account whether the IRS has allowed the taxpayers to claim one or both of their sons as dependents for 2011 federal tax purposes. Even in income tax cases where IRS records are not ambiguous, the Commission will occasionally make an independent review and determine whether an income tax component found in IRS records is correct or not.⁴ As a result, the Commission declines to find from IRS records alone that the taxpayers are not entitled to claim both of their sons as dependents for 2011 Utah tax purposes.

The taxpayers, however, have not shown that they were entitled to claim their older son as a dependent for the 2011 tax year. First, the taxpayers have not shown that they contacted the IRS to correct the erroneous Social Security number they reported for their older son on their 2011 federal return or that the IRS has allowed them to claim both sons as dependents for the 2011 tax year.

Second, even though the IRS has allowed the taxpayers to claim both of their sons for many years prior to 2011 and for the 2012 year subsequent to 2011, they have not shown that the Internal Revenue Code ("IRC") provides that they can claim their older son as a dependent for 2011. "Dependent" is defined in IRC §152(a), in general, to mean a "qualifying child" or "qualifying relative." IRC 152(c)(1) provides several requirements that must all be met before a child is a "qualifying child" whom a taxpayer can claim as a dependent for a particular tax year, as follows:

- (c) Qualifying child. For purposes of this section--
 - (1) In general. The term "qualifying child" means, with respect to any taxpayer for any taxable year, an individual--
 - (A) who bears a relationship to the taxpayer described in paragraph (2),

⁴ See, e.g., *USTC Appeal No. 06-1408* (Initial Hearing Order Nov. 5, 2007); *USTC Appeal No. 08-1313* (Initial Hearing Order Mar. 19, 2009); *USTC Appeal No. 08-0515* (Initial Hearing Order May 14, 2009); *USTC Appeal No. 11-827* (Initial Hearing Order Jul. 12, 2012); and *USTC Appeal No. 14-1809* (Initial Hearing Order Feb. 21, 2017). These and other selected decisions can be reviewed on the Commission's website at <https://tax.utah.gov/commission-office/decisions>.

- (B) who has the same principal place of abode as the taxpayer for more than one-half of such taxable year,
- (C) who meets the age requirements of paragraph (3),
- (D) who has not provided over one-half of such individual's own support for the calendar year in which the taxable year of the taxpayer begins, and
- (E) who has not filed a joint return (other than only for a claim of refund) with the individual's spouse under section 6013 [IRC §6013] for the taxable year beginning in the calendar year in which the taxable year of the taxpayer begins.

At the Initial Hearing, insufficient information was proffered to show that the taxpayers' older son is an individual who met all of the above requirements for the 2011 tax year. Regardless, sufficient information was proffered to show that the taxpayers' older son *did not* meet one of the requirements, specifically the IRC 152(c)(1)(C) "age requirements of paragraph (3)."

IRC §152(c)(3) provides that an individual cannot be claimed by a taxpayer unless the following age requirements are met:

(3) Age requirements.

(A) In general. For purposes of paragraph (1)(C), an individual meets the requirements of this paragraph if such individual is younger than the taxpayer claiming such individual as a qualifying child and--

- (i) has not attained the age of 19 as of the close of the calendar year in which the taxable year of the taxpayer begins, or
- (ii) is a student who has not attained the age of 24 as of the close of such calendar year.

....

The taxpayers' older son turned 19 years of age on January 28, 2011 and, thus, can only meet the age requirement for the 2011 tax year if he is a "student" for this year. In IRC §152(f)(2), "student" is defined, as follows:

(2) Student defined. The term "student" means an individual who during each of 5 calendar months during the calendar year in which the taxable year of the taxpayer begins--

- (A) is a full-time student at an educational organization described in section 170(b)(1)(A)(ii) [IRC §170(b)(1)(A)(ii)], or
- (B) is pursuing a full-time course of institutional on-farm training under the supervision of an accredited agent of an educational organization described in section 170(b)(1)(A)(ii) [IRC §170(b)(1)(A)(ii)] or of a State or political subdivision of a State.⁵

⁵ An IRC §170(b)(1)(A)(ii) educational organization is described as one "which normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on[.]"

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For five months of 2011, the taxpayers' older son was not a full-time student and was not pursuing a full-time course of institutional on-farm training. He was on a church mission for at least 11 months of the 2011 tax year. Because the taxpayers' older son is not considered to be a "student" for the 2011 tax year and because he turned 19 years of age during 2011, the older son does not meet the age requirements of IRC §152(c)(3) for the 2011 tax year. Accordingly, the taxpayers' older son is not a "qualifying child" whom the taxpayers can claim as a dependent for 2011 income tax purposes. For these reasons, the Commission should sustain the Division's 2011 assessment, as reflected in the Second Statutory Notice for the 2011 tax year.

Kerry R. Chapman
Administrative Law Judge

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DECISION AND ORDER

Based on the foregoing, the Commission sustains the Division's 2011 assessment, as reflected in the Second Statutory Notice that the Division issued. The Commission also finds that the taxpayers currently have a \$0 account balance for the 2012 tax year. It is so ordered.

This decision does not limit a party's right to a Formal Hearing. However, this Decision and Order will become the Final Decision and Order of the Commission unless any party to this case files a written request within thirty (30) days of the date of this decision to proceed to a Formal Hearing. Such a request shall be mailed, or emailed, to the address listed below and must include the Petitioner's name, address, and appeal number:

Utah State Tax Commission
Appeals Division
210 North 1950 West
Salt Lake City, Utah 84134

or emailed to:

taxappeals@utah.gov

Failure to request a Formal Hearing will preclude any further appeal rights in this matter.

DATED this _____ day of _____, 2019.

John L. Valentine
Commission Chair

Michael J. Cragun
Commissioner

Rebecca L. Rockwell
Commissioner

Lawrence C. Walters
Commissioner

Notice: If a Formal Hearing is not requested as discussed above, failure to pay the balance resulting from this order within thirty (30) days from the date of this order may result in a late payment penalty.